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Summary of U.S. Economic Conditions

Faltering spending and low consumer and business confidence, together with unfinished major structural adjustments in the financial and nonfinancial sectors, cloud the outlook for a robust economic recovery in the remainder of 1992.

Chief among the uncompleted structural adjustments that have been impeding the economic recovery are the following: high real long-term interest rates, high levels of consumer and business indebtedness, bad debts of savings and loan banks, weak money and credit growth, high interest rates on consumer credit, the depressed value of commercial real estate, large budget deficits on all levels of government, and weak economic growth abroad.

In spite of some improvements in business indebtedness and profits, both business and consumer confidence and spending remain at a low ebb. Since these improvements were largely achieved through wage cutting and employment reduction rather than through job creation and wage expansion, they did not have a broad, positive impact on the economy. At the same time, consumer spending has been weighed down by a high rate of debt accumulation and high interest rates on consumer credit.

Moreover, large fiscal deficits at all levels impeded governments' ability to use fiscal stimuli. Because of large budget deficits, the Federal Government relied largely on monetary policy to propel the recovery. Monetary policy is a weaker stimulus than fiscal policy particularly during periods of stagnation, loss of confidence, and declining asset values. Most financial observers—chief among them, the Federal Reserve—recognize that the drastic cut in key interest rates has failed to spur vigorous economic growth. Low interest rates have helped some businesses and consumers to refinance part of their debts at lower rates, thus reducing their debt burden. Lower interest rates have also widened the spread between interest rates that banks pay to depositors and those rates that banks charge on consumer loans, with the result of boosting bank profit margins. However, in spite of improved profit margins, the bulk of bank lending goes to finance long-term government bonds instead of financing business investment because of the relatively high yield and low risk of government bonds. A drawback of the decline in interest rates has been the reduction of many market-instruments yields to their lowest levels in the past two decades, thus cutting down on consumer and business incomes and spending.

Against this backdrop, the Federal Reserve Board forecasts a 2.0 to 3.25 percent GDP real growth rate, a 3.0 to 3.5 percent inflation rate, and a 7.0 to 7.5 percent unemployment rate for 1992; and a 2.5 to 3.5 percent GDP real growth rate, a 2.5 to 4.0 percent inflation rate, and 6.5 to 7.25 percent unemployment rate for 1993. The assumptions on which these forecasts are based include: a) progress in resolving the various structural adjustments in the financial and nonfinancial sectors, 2) improved commercial real estate prices, 3) progress of business and consumers in straightening their finances and reducing their indebtedness, and 4) a more expansive level of consumer and business spending and investing. Fiscal policies and an open world-trading system are also essential to enhance capital formation and productivity, according to the Federal Reserve Board.

The attitude of business toward a more expansive level of spending seems to have improved slightly. The U.S. Department of Commerce's latest survey of U.S. business-spending plans show that real spending on plant and equipment for all industries should increase by 5.8 percent in the remainder of 1992. Actual spending during the first half of 1992 rose by 3.2 percent from a year ago. Business spending dropped by 1.6 percent in 1991. Most nonmanufacturing industries plan robust gains. Manufacturing industries, however, plan a reduction of 3.0 percent in spending. Primary metals, fabricated metals, nonelectric machinery, and petroleum industries, all anticipate large declines in spending.

In spite of the weak recovery, quarterly statistics released by Commerce show a rise in U.S. productivity. Because of a decline in wages and an increase in hours worked, productivity in the nonfarm business sector expanded at a 2.2 percent annual rate in the second quarter of 1992. The gains in productivity in the second quarter were, however, lower than the gains in the first. Productivity rose by 3.8 percent in the first quarter. Productivity in the manufacturing sector increased by 4.7 percent at an annual rate in the second quarter after declining in the first. Nonfarm business unit labor costs edged up by only 0.7 percent

in the past four quarters, the smallest increase since early 1984. Unit labor costs in manufacturing dropped 1.3 percent in the 1992 second quarter.

Monthly statistics show that job and income losses continued throughout the month of August. Labor Department statistics show that jobs in the private sector fell by 167,000 in August, the largest drop since early 1991. Manufacturing and retail sales suffered most of the job losses. Retail sales, a measure of consumer demand, fell in August by 0.5 percent, following an increase of 1.0 percent in July, according to Department of Commerce data. Car sales declined 1.1 percent, and furniture sales by 2.7 percent. Sales were weak in other sectors like building materials, general merchandise, and food. Commerce data also show that orders for durable goods fell 3.4 percent in July after rising 2.8 percent in June, suggesting sluggish employment growth in the industrial sector. Large declines in orders of transportation equipment, aircraft and parts (15.2 percent), capital goods (10.6 percent), defense goods (26.4 percent), and a lesser decline in orders for both primary metals and industrial machinery and equipment (1.9 percent) accounted for the overall decline in orders for durable goods. In addition, August's industrial production statistics reflect the lingering weakness in the manufacturing sector. Total industrial production dropped by 0.5 percent in August, the biggest drop in 7 months. Part of the decline in the nation's output was caused by the devastating effects of Hurricane Andrew and the effects of a labor strike at General Motors.

Finally, the slow growth in general economic activity was reflected in the slim increase in the index of leading indicators. The index climbed 0.1 percent in July following a decline of 0.2 percent in June and after five consecutive monthly gains. Five indicators of the index contributed to the July increase: building permits, average weekly initial claims for state unemployment insurance, stock prices, vendor performance, and manufacturers' new orders for consumer goods and materials in 1982 dollars. Five indicators made negative contributions: changes in manufacturers' unfilled orders in 1982 dollars, the change in sensitive materials prices, index of consumer expectations, money supply in 1982 prices, and contracts and orders for plant and equipment in 1982 dollars. In contrast, the coincident index, a monthly proxy for economic activity, increased by 0.2 percent in July following a decrease of 0.1 percent in June.

In the foreign sector, the U.S. current account (trade in goods and services plus net receipts of investment income and net unilateral transfers) posted a $17.8 billion deficit in the second quarter, triple the $5.9 billion deficit recorded in the first quarter. The rise in the second quarter deficit was caused by increased imports of merchandise and a decline in net receipts of investment income. Merchandise trade posted a $24.4 billion deficit in the second quarter, up from a $17.2 billion deficit in the first. In contrast, services posted a $13.0 billion surplus. Investment income declined to $1.4 billion in the second quarter, from $4.5 billion in the first. In the capital account, U.S. direct investment abroad rose $11.0 billion in the second quarter whereas foreign direct investment in the United States rose $6.0 billion. Foreign official holdings of U.S. assets, primarily U.S. Treasury securities, rose to tie the record $20.1 billion set in the first quarter. On a monthly basis the U.S. merchandise trade deficit increased by $1.1 billion to $7.8 billion in July. Exports decreased to $37.3 billion in July, and imports increased to $45.2 billion. The January-July trade deficit amounted to approximately $74.5 billion at an annual rate compared with a $65.4 billion deficit in the corresponding period of 1991.

U.S. Economic Performance Relative to Other Group of Seven Members

Economic Growth

Real GDP—the output of goods and services produced in the United States measured in 1987 prices—grew in the second quarter of 1992 at an annual rate of 1.4 percent after climbing in the first quarter of 1992 by 2.9 percent at an annual rate. Real GDP declined by 1.2 percent in 1991, the first annual decline since 1982.

The annualized rate of real economic growth in the second quarter of 1992 was -0.4 percent in the United Kingdom, 0.4 percent in France, -1.1 percent in Germany, and 0.7 percent in Canada. The annualized rate of real economic growth in the first quarter was 3.4 percent in Japan, and 2.4 percent in Italy.

Industrial Production

Seasonally adjusted U.S. industrial production declined in nominal terms by 0.5 percent in August 1992 after a revised increase of 0.6 percent in July. The August decline was due to two factors: 1) the effects of Hurricane Andrew, which reduced the output of gas and petroleum products; and 2) a strike at General Motors, which affected automobile production. Capacity utilization in manufacturing, mining, and utilities decreased by 0.5 percentage points to 78.5 percent in August, from 79.0 percent in July 1992. Total industrial output in August 1992 was 0.6 percent higher than in August 1991. For the second quarter, the index increased at an annual rate of 5.2 percent after falling by 2.9 percent in the first quarter.

Other major industrial countries reported the following annual growth rates of industrial production: For the year ending July 1992, Japan reported a decrease of 6.2 percent and Germany reported a decrease of 2.5 percent. For the year ending June 1992, France reported a decrease of 0.5 percent, the United Kingdom reported a decrease of 2.3 percent, Canada

reported a decrease of 0.7 percent, and Italy reported an increase of 0.9 percent.

Prices

The seasonally adjusted U.S. Consumer Price Index rose by 0.3 percent in August after rising by 0.1 percent in July 1992. The consumer price index rose by 3.1 percent during the 12 months ending August 1992.

During the 1-year period ending August 1992, prices increased 3.5 percent in Germany and 5.2 percent in Italy. During the year ending July 1992, prices increased 1.3 percent in Canada, 2.9 percent in France, 3.7 percent in the United Kingdom, and 1.7 percent in Japan.

Employment

The seasonally adjusted rate of unemployment in the United States declined to 7.6 percent in August, from 7.7 percent in July 1992.

In August 1992, unemployment was 11.6 in Canada and 6.7 percent in Germany. In July 1992, unemployment was 9.7 percent in the United Kingdom, 2.2 percent in Japan, 10.3 percent in France, and 11.1 percent in Italy. (For foreign unemployment rates adjusted to U.S. statistical concepts, see the tables at the end of this issue.)

Forecasts

Forecasts point to moderate real economic growth in the United States for the remainder of 1992, followed by stronger growth in the first half of 1993. Tempering the economic recovery in the remainder of 1992 would be the general slowdown in global economic growth, particularly in industrialized countries, and the uncompleted structural adjustments in the financial and nonfinancial sectors that have been impeding a stronger recovery in the United States. Although U.S. consumer and business indebtedness has eased up a little, loss of jobs and the slowdown in the manufacturing and other sectors have led consumers and businesses to exercise caution in their spending. Table 1 shows macroeconomic projections by four major forecasters for the U.S. economy for July 1992-June 1993 and the simple average of these forecasts. Forecasts of all the economic indicators except unemployment are presented as percentage changes over the preceding quarter on an annualized basis. The forecasts of the unemployment rate are averages for the quarter.

Several factors appear to be working in favor of a stronger growth of about 3.3 percent in the first half of 1993:

- a probable improvement in general economic conditions as the process of adjustment in the business sector continues and as consumer confidence and spending strengthen;

- expected gains in employment and subsequent rise in incomes;

- an expected rise in investment spending because of the moderation of wage increases, cost cutting and corporate restructuring, together with low interest and inflation rates;

- an expected increase in export growth as a result of the relative moderation of the foreign value of the dollar; and

- the anticipated improvement in the industrial countries' economic conditions, which should increase foreign demand for U.S. exports. The average of the forecasts points to a slight decline in the unemployment rate in the last quarter of 1992 and a larger decline in the first half of 1993. Inflation (as measured by the GDP deflator) is expected to decline in the second half of 1992 and to rise a little in the first and, then, to slowdown in the second quarter of 1993.

Table 1
Projected quarterly percentage changes of selected U.S. economic indicators, July 1992-June 1993

Quarter	UCLA Business Forecasting Project	Merrill Lynch Capital Markets	Data Resources Inc	Wharton E.F.A. Inc.	Mean of 4 forecasts
			GDP current dollars		
1992					
July-September	5.0	4.4	3.6	5.1	4.5
October-December	5.3	5.4	4.9	5.7	5.3
1993					
January-March	6.4	6.2	6.4	6.7	6.4
April-June	6.9	5.9	6.6	6.0	6.3
			GDP constant (1987) dollars		
1992					
July-September	2.0	1.5	1.8	2.5	1.9
October-December	2.0	2.8	2.9	2.9	2.7
1993					
January-March	3.2	2.9	3.3	3.2	3.2
April-June	3.7	3.0	3.7	3.0	3.3
			GDP deflator index		
1992					
July-September	2.9	2.9	1.7	2.6	2.5
October-December	3.2	2.5	2.0	2.8	2.6
1993					
January-March	3.1	3.2	2.9	3.4	3.1
April-June	3.3	2.8	2.8	2.9	2.9
			Unemployment, average rate		
1992					
July-September	7.6	7.5	7.7	7.8	7.7
October-December	7.6	7.4	7.6	7.7	7.6
1993					
January-March	7.5	7.2	7.4	7.5	7.4
April-June	7.2	6.9	7.2	7.3	7.1

Note.—Except for the unemployment rate, percentage changes in the forecast represent compounded annual rates of change from preceding period. Quarterly data are seasonally adjusted. Date of forecasts: August 1992.

Source: Compiled from data provided by The Conference Board. Used with permission.

U.S. TRADE DEVELOPMENTS

The seasonally adjusted U.S. merchandise trade deficit rose from $6.7 billion in June to $7.8 billion in July 1992. A $900-million drop in July's exports and a $300-million increase in imports accounted for the $1.1-billion worsening in the monthly balance. Exports decreased to $37.3 billion in July, and imports increased to $45.2 billion. The trade deficit increased to $43.4 billion in January-July 1992, from $36.1 billion in the corresponding period of 1991. At an annual rate, the deficit increased from $62.0 billion in January-July 1991 to $74.5 billion in the corresponding period in 1992. Seasonally adjusted U.S. merchandise trade in billions of dollars as reported by the U.S. Department of Commerce is shown in table 2.

The July 1992 deficit was 30 percent higher than the $6.0-billion average monthly deficit registered during the previous 12-month period and 39 percent higher than the $5.6-billion deficit registered in July 1991. When oil is excluded, the July 1992 merchandise trade deficit increased by $1.0 billion from the previous month.

Nominal export changes and trade balances in July 1992 for specified major commodity sectors are shown in table 3. All sectors recorded export decreases from June to July. The largest export drops were in airplanes followed by those in vehicle parts. Airplanes, however, recorded the largest trade surplus in the January-July 1992 period.

The U.S. agricultural trade surplus rose in July from June at $1.3 billion. The agricultural surplus reached $10.1 billion in January-July 1992 and was running 17.4 percent above the level recorded in the January-July 1991 period ($8.6 billion). The U.S. oil import bill increased from $3.5 billion to $3.8 billion.

U.S. bilateral trade balances on a monthly and year-to-date basis with major trading partners are shown in table 4. In July 1992, the United States registered an increase in bilateral merchandise trade deficits with Japan, Germany, the European Free Trade Association (EFTA), the Organization of Petroleum Exporting Countries (OPEC), the Newly Industrializing Countries (NICs), and China. The U.S. deficit with Japan increased by $540 million. From January-July 1991 to the corresponding period in 1992, the United States registered a significant decline in its bilateral trade deficit with OPEC and deficit increases with Japan, Canada, Germany, EFTA, the NICs, and China.

The U.S. trade surpluses with the EC and Western Europe declined, and the trade surpluses with Mexico and the former USSR increased.

Table 2
U.S. merchandise trade, seasonally adjusted

(Billion dollars)

	Exports		*Imports*		*Trade balance*	
Item	*July 92*	*June 92*	*July 92*	*June 92*	*July 92*	*June 92*
Current dollars—						
Including oil	37.3	38.2	45.2	44.9	-7.8	-6.7
Excluding oil	36.7	37.6	40.3	40.1	-3.6	-2.6
1987 dollars	35.4	36.0	42.5	42.3	-7.1	-6.3
Three-month-moving average	37.1	36.8	44.3	43.7	-7.2	-7.0
Advanced-technology products (not seasonally adjusted)	8.1	9.6	5.9	6.2	+2.1	+3.4

Source: *U.S. Department of Commerce News, (FT 900)*, September 1992

Table 3
Nominal U.S. exports and trade balances, not seasonally adjusted, of specified manufacturing sectors and agriculture, January 1991-July 1992

Sector	Exports: January-July 1992	Exports: July 1992	Change: January-July 1992 over January-July 1991	Change: July 1992 over June 1992	Share of total January-July 1992	Trade balances January-July 1992
	Billion dollars		Percent			Billion dollars
ADP equipment & office machinery	15.3	2.0	1.3	-16.7	5.9	-4.30
Airplanes	16.2	1.7	21.1	-37.9	6.3	14.02
Airplane parts	5.5	0.8	-4.8	-5.0	2.1	3.42
Electrical machinery	18.3	2.5	4.8	-6.3	7.1	-3.86
General industrial machinery.	11.0	1.5	10.6	-12.4	4.2	1.75
Iron & steel mill products	2.1	0.3	-14.4	-10.0	0.8	-2.76
Inorganic chemicals	2.5	0.4	4.6	0	1.0	0.41
Organic chemicals	6.5	1.0	-4.0	-8.0	2.5	1.33
Power-generating machinery	10.2	1.4	6.6	-11.9	3.9	1.23
Scientific instruments	8.4	1.1	7.1	-5.0	3.2	4.15
Specialized industrial machinery	9.7	1.4	-1.0	-7.3	3.7	3.01
Telecommunications	6.2	1.0	11.3	-7.0	2.4	-7.67
Textile yarns, fabrics and articles	3.4	0.4	8.1	-14.0	1.3	-1.25
Vehicle parts	9.6	1.1	19.6	-31.9	3.7	0.47
Other manufactured goods[1]	16.1	2.3	14.4	-5.8	6.2	-2.57
Manufactured exports not included above	60.9	8.5	7.1	-7.9	23.5	-48.57
Total manufactures	202.0	27.2	7.3	-12.5	77.9	-41.19
Agriculture	24.1	3.2	10.6	-0.3	9.2	10.12
Other exports	33.4	5.1	-0.9	6.7	12.9	-7.89
Total	259.5	35.5	6.5	-9.2	100.0	-38.96

[1] This is an official U.S. Department of Commerce commodity grouping.

Note: Because of rounding, figures may not add to total shown.

Source: *U.S. Department of Commerce News, (FT 900)*, September 1992.

Table 4
U.S. merchandise trade deficits (-) and surpluses (+), not seasonally adjusted, with specified areas, January 1991-July 1992.

(Billion dollars)

Area or country	July 1992	June 1992	July 1991	January-July 1992	January-July 1991
Japan	-3.93	-3.39	-3.80	-25.79	-22.91
Canada	-0.38	-0.42	-0.49	-3.63	-2.95
Western Europe	-1.15	-0.09	-0.05	+6.93	+11.00
EC	+0.79	+0.09	+0.19	+8.24	+11.23
Germany	-0.78	-0.72	0.22	-3.32	-2.14
European Free Trade Association(EFTA)[1]	-0.53	-0.41	-0.34	-2.22	-1.14
NICs[2]	-1.71	-0.86	-1.71	-7.03	-6.00
USSR (former)	+0.24	+0.23	+0.12	+1.62	+1.40
China	-2.10	-1.47	-1.29	-9.27	-5.89
Mexico	+0.63	+0.33	+0.45	+3.73	+1.05
OPEC	-1.47	-1.10	-1.10	-5.23	-8.50
Total trade balance	-10.14	-6.61	-7.85	-38.95	-31.78

1 EFTA includes Austria, Finland, Iceland, Liechtenstein, Norway, Sweden, and Switzerland.

2 NICs includes Hong Kong, the Republic of Korea, Singapore, and Taiwan.

Note.— Country/area figures might not add to totals because of rounding. Also, exports of certain grains, oilseeds and satellites were excluded from country/area exports but were included in total export table.

Source: *U.S. Department of Commerce News, (FT 900)*, September 1992.

INTERNATIONAL TRADE DEVELOPMENTS

U.S.-EC oilseeds dispute: Where are we now?

Although threats of retaliation and counterretaliation have been fired across the Atlantic throughout the summer, the U.S.-EC dispute over Community subsidies on oilseeds remains unresolved. The findings of two GATT dispute settlement panels have condemned the EC's policies on oilseed subsidies, but adequate reforms have not been forthcoming. Most recently, the EC has offered compensation to the United States under GATT article XXVIII.

For 4 years, the United States has been actively challenging the GATT consistency of the EC's oilseeds subsidy program and seeking its reform. In 1988, the GATT established a panel at the request of the United States to examine EC subsidies to processors and producers of oilseeds and related animal-feed proteins. The United States claimed that the EC's subsidies denied U.S. exporters the benefits of duty-free access (zero tariffs) to the EC market that had been agreed upon in the Kennedy Round of trade negotiations in 1962. The panel report, adopted in January 1990, supported the U.S. claims and recommended that the EC bring its subsidy program into compliance with the GATT.

Although the EC proposed a reform of its oilseeds subsidies under the Common Agricultural Policy (see *IER*, May 1992), the United States asserted that the new plan would continue to impair the benefits that should accrue as a result of the duty-free bindings on oilseeds. Consequently, the original dispute-settlement panel reconvened in December 1991 to determine whether the EC's proposed reforms conformed to the panel requirements. The panel, which issued its "followup" findings in March 1992, again supported the U.S. position. It declared, that if the EC did not eliminate the impairment by either modifying its new subsidy program or providing compensation, the United States should be granted authority by GATT members to withdraw concessions unilaterally to offset the trade losses.

With U.S. patience fading, on April 30 the United States Trade Representative (USTR) announced its intention to raise tariffs on $1 billion of imports from the EC in retaliation for the EC's failure to comply with the GATT panel's findings. On June 12, the USTR published a list of products in the *Federal Register* representing $2 billion in U.S. imports from the EC and, from which the final list of products subject to retaliation would be identified. The list included a wide variety of products: cheese, cut flowers, vegetables, sausages, seafood, candy and other confectionery products, nuts, fruit juices, wine and other alcoholic beverages, certain animal feeds, and tobacco products. Despite this move, U.S. officials said they still hoped an acceptable solution would be forthcoming.

At the June 19 meeting of the GATT Council, the EC was authorized under GATT article XXVIII:4 to begin talks with the United States and other oilseed exporting countries, aimed at compensating them for damage caused by the EC's oilseeds subsidies. GATT rules allow the EC to retain its current oilseeds program if compensation, such as lower tariffs in other sectors, is provided. The United States warned the EC that compensation would be costly, namely, $1 billion in compensation to the United States for lost oilseeds sales and another $1 billion to other countries. Other exporters of oilseeds involved in the negotiations include Brazil, Argentina, and Canada.

Under article XXVIII:4, the EC had 60 days to find a satisfactory solution. In July, the EC offered a compensation package that the United States rejected as inadequate in addressing the impairment faced by U.S. farmers. A second compensation offer was presented by the EC in August, but the United States also rejected it as insufficient. Neither package included the dismantling of the EC's oilseeds subsidy regime, which the United States and other oilseed exporters consider vital in any settlement.

As the 60-day deadline approached, threats of retaliation and counterretaliation escalated. EC officials claimed that any retaliation by the United States would be GATT illegal. Ray MacSharry, EC Commissioner for Agriculture and Rural Development, said, "I hope that the U.S. will abide by GATT rules in this matter as, clearly, if the U.S. proceeds to take unilateral action against Community imports,...the Community would have to retaliate against such action." EC officials continue to claim that U.S. exports to the EC have declined because they have been replaced by imports from other oilseed-producing countries.

Although the 60-day deadline passed without agreement, the United States postponed retaliation. Under GATT rules, if no settlement is reached within

60 days, the GATT Council will make a determination. Should the Council decide that the EC has failed to offer adequate compensation, the United States has the right to retaliate.

At the next GATT Council meeting on September 29, the United States proposed binding arbitration by an independent panel to determine the amount of compensation the EC should provide to its trading partners for lost oilseed sales. However, the EC rejected the U.S. proposal and instead backed a plan to set up a GATT working party. The two parties are currently negotiating a settlement to this procedural issue. The United States has again postponed retaliation: progress on the long-stalled Uruguay Round negotiations is closely tied to the outcome of the oilseeds talks.

Are the United States and China on the Brink of a Trade War?

On August 21, United States Trade Representative (USTR) Carla Hills released a list of Chinese products targeted for possible tariff rate increases of up to 100 percent *ad valorem* if China fails to remove barriers to U.S. exports. This preliminary list, which is subject to public comment and hearings, accounted for U.S. imports from China of $3.9 billion during 1991. The announcement was made after an agreement could not be reached during the fifth round of high-level bilateral negotiations held in a market-access investigation initiated by the USTR last October under section 301 of the Trade Act of 1974. If an agreement is not reached by October 10, 1992, the scheduled deadline for concluding the investigation, the President must decide whether to impose the punitive duties. Chinese officials have responded to the possible retaliation, the largest yet threatened under U.S. law, by saying that they would also increase tariffs to prohibitive levels on 4-billion dollars' worth of U.S goods.

The current U.S. list of products will be reduced but kept at a level high enough to compensate for the estimated losses of U.S. exporters because of Chinese import barriers. In developing the final list, the USTR has pledged to make efforts to minimize the negative impact that a decision to increase tariffs would have on U.S. producers, workers, and consumers. The present list covers a cross section of products that include leading Chinese exports to the U.S. market: footwear; electrical appliances and electronics goods; handtools and industrial hardware; handbags, luggage, and other articles of plastic or leather; food products; and silk apparel. Most textiles and apparel, the largest commodity group among U.S. imports from China, were not included because access to the U.S. market is already limited under a bilateral agreement. Also, most toys were exempt because a number of U.S. toy companies rely almost entirely on imports from China. China's retaliation list could include, according to Chinese officials, most of the major U.S.-produced goods it imports: commercial aircraft and aircraft parts; fertilizers and other chemical products; computers; and medical and other analytical instruments. Wheat, one of the leading U.S. exports to China, reportedly would not be included; however, China has said it will stop buying U.S. wheat unless President Bush rescinds his recent decision to sell F-16 fighter planes to Taiwan.

Total U.S. imports from China amounted to $18.9 billion in 1991, making China the United States' sixth most important import source. On the other hand, U.S. exports to China amounted to only $6.2 billion, leaving a U.S. bilateral deficit of $12.6 billion. Based on an extrapolation of U.S.-China trade during the first 6 months of this year, the deficit could reach nearly $15 billion in 1992.

At issue in the U.S. market-access complaint is a broad spectrum of Chinese trade practices. In particular, the United States charges that four types of import barriers impede the access of U.S. exporters to the Chinese market: the prevalence of unpublished or unclear regulations governing China's imports; import bans and quantitative restrictions; restrictive import-licensing requirements; and standards and testing requirements that act as trade barriers, especially in the agricultural area. The United States also is pressing for reductions in China's excessively high tariff rates, some of which range from 120 to 140 percent *ad valorem*, and further contends that its import substitution policy effectively prohibits the entry of many goods.

Despite the failure to reach an agreement thus far, some progress has been made toward resolving all of these issues (*IER*, July 1992). In January 1992, China began publishing previously secret import regulations and, during a round of negotiations in July, agreed to invalidate the presumably hundreds of unpublished laws, regulations, and administrative guidelines governing its trade. Regulations to that effect must be issued, however, and China has not yet done so. It reduced tariffs on 225 products at the beginning of 1992 and in May provided the United States with a list of 50 more products whose tariffs would be cut. During the July talks, China also provided complete lists of the products subject to import bans and quotas and promised to eliminate specific categories of these import restrictions. It furthermore pledged to gradually eliminate the import licensing requirements that most affect U.S. exports and to abolish its import substitution measures and guidelines "over time." Before an agreement, or memorandum of understanding, can be concluded, however, the two sides must agree on a timeframe or series of deadlines that China will follow in carrying out its commitments. The United States has also indicated that it intends to formally monitor the implementation of these commitments.

Although another round of bilateral talks ended in failure on September 17, U.S. negotiators remain hopeful that the two sides can conclude an agreement

during the final talks that are scheduled to begin on October 1 and may continue until the October 10 deadline. China conceded to U.S. demands in a similar last-minute showdown in January of this year when the United States threatened to impose punitive tariffs unless the Chinese Government substantially strengthened its protection of U.S. intellectual property rights (*IER*, February 1992). Both sides reportedly assumed a more conciliatory position during the September talks, but China stands to lose much more than the United States if agreement cannot be reached and a trade war breaks out. The U.S. market accounts for about 25 percent of China's annual exports, but less than 2 percent of U.S. exports go to China. Moreover, the United States has made it clear throughout the negotiations that the trade reforms China would be agreeing to make are among those that will likely be required to regain membership in the General Agreement on Tariffs and Trade (GATT). (China was a charter member of GATT, resigned after the Communists came to power, and reapplied in 1986). During the past year, GATT membership has emerged as a major goal of the Chinese Government, given the increasingly important role of the country in the international economy and its reliance on exports to fuel domestic growth.

NAFTA Up North: Canadian Reaction to the Trade Agreement

Within Canada the subject of free-trade agreements, laden with heavy political baggage, is certain to elicit a strong response whether the interlocutor is in favor of or against regional attempts at trade liberalization. In 1988 the United States and Canada, the two largest trading partners in the world, agreed to enter into a free-trade arrangement under which duties between the two countries would be completely eliminated over a 10-year period starting on January 1, 1989. Shortly after the inception of the FTA, an economic downturn began, and both countries are still suffering from its effects. A national election was fought over the U.S.-Canada Free Trade Agreement (CFTA) in 1988, and Brian Mulroney successfully defended the agreement and his Government's close association with it. In the election, his Conservative Party swept to a substantial majority in the Canadian Parliament, and the CFTA was subsequently ratified. Nevertheless, the CFTA has been held responsible for a number of negative economic developments since 1990 by those Canadians who were against the trade pact from the start.

When Mexico and the United States decided to enter into negotiations toward another bilateral FTA in June 1990, Canada did not want to see any of the gains that it had negotiated eroded, nor did it wish to see the United States become the sole North American trader to have a free-trade relationship with its continental neighbors. This concept of what was later referred to as the "hub-and-spoke" system of interlocking alliances (with the United States as the hub) was viewed as detrimental to Canadian interests. What began as a bilateral negotiation between Mexico and the United States was broadened in February 1991 into a trilateral effort including Canada.

The recent announcement of the completion of negotiations for a North American Free-Trade Agreement (NAFTA) has started another round of consideration and evaluation of the terms of the agreement as well as an exploration and a revisitation to the ideal of a regional free-trade agreement. The analysis will take place in the highly charged political atmosphere of an election year in the United States, and the Canadian environment is no less agitated. Canada is embroiled in a national focus on constitutional issues triggered by Quebec's threat to effectively sever its ties with the Canadian federation, and another national election looms in the background. [Canada observers expect that national elections will take place in the spring of 1993.] Whereas Mexico is viewed in the popular press as the clear "winner" in the NAFTA sweepstakes, Canada is considered a rather uncertain and uneasy partner. Given the strong anti-FTA sentiment in Canada and the low popularity ratings of the federal government, the outcome of the NAFTA debate is far from certain. The timing of a call for a general election, if it occurs when the NAFTA will be the center of parliamentary debate next spring, would ensure that the free-trade agreement itself would become the crucial issue in the election campaign, a replay of 1988.

The constitutional question is currently at the front and center of the national debate in Canada, with the economy another important, although secondary, consideration. NAFTA serves as a lightning rod for concern about the effects of recession and the loss of manufacturing jobs. Lingering resentment over the CFTA will definitely color the NAFTA debate in Canada. However, it is argued in certain circles that ratification of NAFTA is necessary if Canada does not want to be left behind in a hemispheric drive toward closer association and the construction of a broad regional trade bloc.

CFTA versus NAFTA

An important question to Canadians is how the 1989 CFTA will be affected by NAFTA. The new agreement has been officially described as "FTA-plus" because it effectively acknowledges and incorporates the provisions of the existing CFTA while it also enhances some of the CFTA's stipulations. The basic elements of the 1989 bilateral accord remain intact. The accord includes the CFTA's exemptions for Canadian cultural industries and commodities governed by supply-management policies. The CFTA timetable for the mutual elimination of duties between the United States and Canada remains untouched by NAFTA. The Canadian Government has already

acknowledged that implementation of the new accord would not require a host of legal changes because the provisions of NAFTA closely "parallel" the CFTA, which has already been incorporated into Canadian law.

Issues

The following is a brief examination of some of the salient points of the NAFTA agreement of particular concern to Canada with a view to any differences between the CFTA and the newly negotiated agreement. (For a description of the CFTA, see U.S. International Trade Commission, *Operation of the Trade Agreements Program, 1987*, USITC publication 2095, July 1988, available by request from USITC, Office of Economics, 500 E Street, SW, Washington, DC 20436.)

Auto Trade

As was the case with the CFTA, the 1964 Auto Pact, which governs trade in automobiles and original equipment parts between Canada and the United States, remains in place under NAFTA. Motor vehicle production, a major industry in Canada, accounts for over half of U.S.-Canadian commerce. The new agreement alters the content requirements for North American cars from the standard contained in the CFTA. The result is that the 50 percent CFTA rule will be increased to 62.5 percent in two stages. Canada had argued for a lower domestic content rule in order to assuage Japanese auto manufacturers who had invested heavily in Canada. The Big Three (Chrysler, Ford, and General Motors)—dominant in both Canada and the United States—had insisted on significantly higher domestic content requirements. The 62.5 percent figure was a compromise. The precision with which domestic content is determined has been refined by using more specific and practical language; clearer terms should lessen the likelihood of unilateral decisions by customs officials in any NAFTA country and may result in the elimination of the Honda Civic dispute between Canada and the United States by a retroactive application of the newly crafted domestic content rules. (U.S. Customs required Honda to pay $22 million in duties as a result of a determination that found certain cars not meeting the requisite percentage of domestically manufactured parts, and thereby dutiable at a higher rate than that accorded most vehicles under the CFTA.)

Agriculture

No trilateral agreement was possible in the agricultural sector. As a result, Canada signed a separate bilateral accord with Mexico, and the CFTA continues to govern trade in agriculture between Canada and the United States. Thus, Canada's protection for its dairy, poultry, and egg sectors continues, as does Canada's right to resort to snap-back provisions for reinstating tariffs in order to correct market distortions in agriculture.

Intellectual Property Rights

Canada's exemption of cultural industries in the CFTA is left untouched by the NAFTA. This enshrines one of Canada's most deeply held positions and can be considered a definite Canadian gain. The issue of Canadian compulsory licensing, particularly in the pharmaceutical sector, has been an ongoing bilateral difficulty between the United States and Canada. The terms of NAFTA will clarify licensing requirements in a way that eliminates the bilateral problem. The level of intellectual property protection under the new accord is higher than that contained in any previous agreement, bilateral or multilateral.

Rules of Origin

Autos and textiles are areas where rules of origin are specifically defined in NAFTA. Preferential treatment within the free- trade area is made conditional on a specific degree of production having been performed in North America. Otherwise, the change of tariff classification rule in the CFTA continues to apply.

Dispute Settlement

The process by which bilateral disputes are addressed by a binational panel will continue under NAFTA. Thus, the mechanism that is considered one of Canada's most significant gains under the CFTA is preserved. (See *IER*, April 1992, p. 10.) The system has been strengthened to ensure that panel decisions are implemented. Inclusion of banking and financial services to the industries covered by the trade dispute mechanisms established under the NAFTA is an advance over the CFTA. Another innovation is the setting out of clear grievance procedures in customs matters, along with the elaboration of how customs audits will be interpreted by working groups established under the dispute settlement process.

Textiles and Apparel

Beyond the rules of origin changes already referred to, NAFTA expands Canadian access to the U.S. market by allowing for additions to the existing tariff rate quotas for wool and nonwool apparel, fabrics, and yarns. Increases to the quotas are also enshrined in the agreement. This provision allows for increased market access for Canadian textiles products that do not meet the rules of origin requirement. NAFTA's requirement that only goods made from cloth woven in North America could receive the benefit of the agreement was opposed by certain Canadian apparel manufacturers.

Canadian Reaction

Reaction to the NAFTA has been largely predictable. Big business, which was a major supporter of the CFTA and stands to gain from the NAFTA, has come out solidly for the accord. Labor, some consumer groups, and the opposition political parties have warmed up their earlier critiques of the CFTA for the NAFTA debate. Their arguments may hold greater sway now in the fourth year of anemic economic performance.

Most business groups in Canada have welcomed the new agreement. Endorsements for the hemispherewide accord have come from the Canadian Chamber of Commerce, the Canadian Manufacturers Association, the Canadian Federation of Independent Business, the Canadian Exporters' Association, and the Business Council on National Issues. The Automotive Parts Manufacturers Association of Canada is strongly supportive of the deal. The Canadian Chemical Producers Association applauded Mexico's willingness to drop state controls over a range of petrochemical products in the agreement. The Canadian Federation of Agriculture president found little change between CFTA and NAFTA. Support was not, however, unanimous as some sectoral groups, such as the Canadian Apparel Manufacturers Institute, expressed concern that NAFTA will present definite difficulties, for instance, meeting the domestic content rules for textiles. A spokesman for the Canadian Textile Institute, on the other hand, expressed the opinion that NAFTA was better than CFTA for the textile industry.

While acknowledging that the agreement creates a "consumer heaven" by breaking down barriers and encouraging competition, the Consumers Association of Canada maintains that the NAFTA is front-end loaded with concessions for business in the early phases of the agreement, with consumers benefitting only as the pact comes into complete implementation and duties are totally eliminated.

The major opposition parties in Canada have generally taken positions against the NAFTA. The opposition Liberal Party is split: its nationalist wing is strongly against the agreement, while its probusiness wing has traditionally supported free trade. The New Democratic Party (NDP) that now holds power in three provinces (Ontario, British Columbia, and Saskatchewan) is strongly anti-NAFTA. In the 1988 election, it promised to abrogate the CFTA if elected. It is joined in its opposition to the pact by a number of vocal groups, including organized labor, the Canadian Labour Congress, and the Canadian Federation of Labour. In this area, Canadian opposition to the trade pact mirrors the reaction of organized labor in the United States.

Conclusion

While most press reports in this country have been focusing on Mexico's gains under the pact and on the American reaction to the agreement, particularly the short-term unskilled job loss in the United States that has come to be associated with the NAFTA, the Canadian reaction has been greatly overlooked. Many believe that Canada, of the three NAFTA participants, will have the most difficult time of ratifying the agreement and implementing its provisions. The fast track process in this country is just beginning with its formal notification, resolute number of days, and legislative calendars. A comparable process for the examination and ratification of the agreement is taking place in Canada. It, however, is being played out against the background of a very serious and intense national discussion of constitutional reform. [A constitutional accord was recently struck between the Federal Government and the premiers of the Canadian provinces. In brief, the accord affects and clarifies the special status of Quebec, the rights of native peoples, and the representation within the Canadian Senate. A national referendum on the accord is scheduled to take place across Canada on October 26, 1992.]

The relationship between the constitutional accord and the NAFTA is purely political. Approval of the former could enhance acceptance of the latter. The Canadian Government has recently allocated $2.5 million for a public relations effort to sell the NAFTA to skeptical Canadians over the next few months. The interplay of these two pivotal issues in Canada will be interesting to watch and could have repercussions on the eventual outcome of the NAFTA pact in the United States.

Japan Proposes Economic Stimulus Program

In the midst of a serious economic downturn and a crisis in the financial sector, Japan's ruling party has proposed a massive spending program to boost an ailing stock market and help spark economic recovery. If fully implemented, the program could have ramifications for Japan's trade balance with the United States and other major trading partners.

On August 28, 1992, Japan's ruling Liberal Democratic Party (LDP) announced an $84 billion (¥10.7 trillion) economic stimulus program designed to push the Japanese domestic economy out of its current recession. The "Crisis Management Program" proposed by the LDP is some $14 billion larger than estimates leaked to the press in earlier weeks and constitutes the largest fiscal stimulus package in Japanese history. The move was prompted by a plummeting Tokyo Stock Exchange, falling economic indicators, and growing trade surpluses with the United States, Western Europe, and other major trading partners.

Japan's economy first showed signs of entering a recession in September 1991, when economists at Japan's Economic Planning Agency (EPA) noted a slowing in the pace of Japan's economic expansion. By January 1992, the EPA had declared the Japanese economy to be in an "adjustment phase" following one of the nation's longest periods of continuous economic growth. Companies that had engaged in high levels of investment during the boom period soon found this

strategy to be unsustainable when interest rates rose, share prices fell, and domestic consumption slowed. Corporate profits in Japan have dropped considerably during the past year, and firms have responded with a variety of cost-cutting measures—many of which have further contributed to the downturn. Pessimism is reportedly high among business and consumers. Some Japanese economists estimate that even a 3.5 percent real growth rate for 1992 will be difficult to achieve. Other economists have been far more pessimistic—predicting a real growth rate of 2 percent or less for 1992. Although such growth rates may look impressive compared to the anemic economies of Western Europe and the United States, they pale in comparison to those achieved during Japan's latest expansion phase.

Contributing to Japan's downturn has been a chaotic situation in the financial sector. The current fragility of Japan's financial sector poses the risk of genuine economic collapse—a situation far worse than the present cyclical downturn. By some estimates, Japanese banks are burdened with ¥60 trillion (approximately $461.5 billion) in bad loans. Additionally, the fall in the Tokyo Stock Market has eaten away at banks' capital. Although the LDP's Crisis Management Plan contains no provisions for rescuing the financial sector, Japanese banks will benefit indirectly from the fiscal stimulus package insofar as its boost to the stock market shores up their capital positions. Nevertheless, there is broad speculation that the Government of Japan will soon have to take more forceful action.

In contrast to these apparently gloomy conditions on the domestic front, Japan has sustained significant increases in bilateral trade surpluses with nearly all major trading partners. According to recent estimates, Japan's external surplus is poised to exceed $100 billion by the end of 1992. Both the trade and current account figures are likely to set new highs in terms of absolute magnitude, and the ratio of the current account surplus to GNP is once again approaching 3 percent, on par with levels seen in the early 1980s. Japan's external balances have improved almost across the board during the first half of 1992 (table 5), mainly because of sharp export gains. In dollar terms, Japan's exports during the first half of 1992 increased by roughly 8.3 percent over the same period in 1991. A similar increase of 7.7 percent was seen in the yen value of Japanese exports.

Japan's rising export gain was broad-based, with higher sales in most major regions—North America, Western Europe, Latin America, and East Asia. According to some economists, the surge in the value of Japanese shipments during the first half of 1992 is at least partly due to a 6.2 percent year-to-year increase in unit dollar prices. A second factor is the strengthened yen. Roughly 40 percent of Japanese exports are presently priced in yen. With the yen having risen in value by roughly 5.1 percent relative to the dollar in the past year, approximately 2.0 percent of the value change in Japanese exports worldwide can be attributed to currency translation.

The import side of the equation is equally important in explaining Japan's rising trade surplus. The volume of overall imports into Japan has slowed progressively over the past several years. Thus far in 1992, the volume of imports into Japan is barely registering positive growth. It is quite likely that this phenomenon is a reflection of Japan's current economic downturn and consequent loss of business and consumer confidence.

The United States continues to be the largest single deficit trader with Japan, although Western Europe is running a bilateral deficit nearly as large. For the first six months of 1992, the U.S. deficit with Japan was estimated at $21.9 billion, an increase of 10.4 percent over the same period in 1991 (table 6). U.S. exports to Japan during the first two quarters of 1992 dropped by roughly 2.5 percent from the previous year's levels. Declines were particularly notable in iron, steel and other metals, fabrics, and electric machinery. Significantly, the noticeable drop in Japanese imports of iron, steel, and other industrial imports would seem to indicate that Japanese companies, concerned about profit margins during the current recession, are running down existing inventories. U.S. imports from Japan, however, climbed by 3.4 percent, led by automobiles and consumer electronics.

Table 5
Japan's trade balance (customs clearance basis) with selected partners
(Millions of Dollars)

Trade balance	*1989*	*1990*	*Jan.-June 1991*	*Jan.-June 1992*
Balance of Payments Trade Balance:				
World	76,917	63,528	44,081	62,884
Exports (f.o.b.)[1]	269,570	280,374	146,968	159,129
Imports (f.o.b.)	192,653	216,846	102,887	96,245
Customs Clearance Trade Balances:				
World	64,328	52,149	32,177	49,033
United States	44,942	37,953	15,883	18,590
Western Europe	21,368	20,715	15,458	17,798
China	-2,630	-5,924	-2,676	-2,425
Taiwan	6,442	6,934	3,807	5,041
Hong Kong	9,307	10,899	6,611	8,420
Singapore	6,287	7,137	4,332	4,406

[1] Figures for Japanese imports and exports obtained from the Japan Economic Institute.
Source: U.S. Department of State.

Table 6
U.S.-Japan merchandise trade balance

(Millions of dollars)

Time period	*Exports*	*Imports*	*Trade Balance*
1989	43,863	93,532	-49,863
1990	47,977	89,667	-41,690
1991:	47,492	91,599	-44,107
I	12,068	23,079	-11,011
II	11,656	21,034	-9,378
III	11,821	23,360	-11,539
IV	11,947	24,126	-12,179
1992:			
I	11,886	22,560	-10,674
II	10,937	22,160	-11,223

Source: U.S. Department of Commerce

The Crisis Management Program introduced by the LDP is mainly intended to spur domestic demand. However, some provisions could slow the worsening U.S.-Japan trade balance. The central pillar of the plan is a proposed $36-billion expenditure program by national and local governments for public works projects, such as highways, sewers, hospitals and recreation facilities. Such a boost to business activity in Japan could indirectly increase imports of American goods and services. The United States has not, however, traditionally held a strong export position vis-à-vis Japan in goods and services related to construction and infrastructure development.

The LDP's proposed stimulus package also contains provisions for additional import promotion programs similar to those announced in previous years. A yet undetermined amount of funds will be allocated for the improvement of trade-related infrastructure (terminals, ports, etc.), and to advance the development of foreign access zones (that is, areas designated for import promotion). The LDP also plans to strengthen the import promotion programs of the Japan External Trade Organization (JETRO) and to expand financing facilities as a special measure to promote imports (this would include lowering interest rates on loans by the Japan Development Bank and by other financing institutions for investments to improve capacity and on manufactured product import loans by the Japan Export-Import Bank).

Although most economists agree that the proposed plan could not help but have an impact on Japan's slowing economy, disagreement remains as to just how much growth it can trigger and to what degree it will affect Japan's external trade surplus. Only part of the total fiscal package will actually find its way into public works spending. At least 18 percent of the funds designated for expansion of public works investment will go towards purchases of land and will likely have little impact on GDP. Additionally, the Diet will probably not pass the supplementary budget until late October, and only about 30 percent of the money will be spent between now and next March, when the Japanese fiscal year ends.

Additionally, some economists argue that Japan's import structure has changed in the past 2 years to reflect a leveling-off of Japanese consumers' propensity to purchase imported goods. Indeed, these economists argue that the increase in Japan's propensity to import registered in the late 1980s was symptomatic of a luxury consumption boom that has since faded. Now, they predict, Japan will return to a more "typical" relationship between income and consumption. If this is the case, an economic stimulus package alone will not do much to raise the level of imports from the United States and other major trading partners.

In one respect, the LDP's economic stimulus plan has already succeeded. Through a carefully organized series of leaks to the press, the Government of Japan has sparked a revival on the Tokyo Stock Exchange, which had been in a near free-fall. By the time the official plan was released on August 28, the Nikkei stock index stood at 18,120.43 points, or roughly 27 percent higher than the market low for this year, which occurred just nine trading days earlier. By September 18, the Nikkei had dropped slightly to 17,944.7 points.

The Economic Consequences of the Czech and Slovak Split

The split of the Czech and Slovak Federal Republic (CSFR) into two independent states, each recognized as a separate entity under international law, is proceeding on schedule. While the two new national governments are being built up, a down-sized, interim federal government continues to exercise some countrywide responsibilities, including joint diplomatic representation and defense. Beginning in 1993, the two countries will have separate budgets and are expected to embark on divergent fiscal, monetary, and economic reform policies.

Analysts foresee a decline in the close-knit cooperation between Czechs and Slovaks in the immediate future. At present, more than one-third of

Slovakia's total industrial output is exported to the Czech lands (Bohemia, Moravia, and part of Silesia) and about one-tenth of the Czech products are exported to Slovakia. Slovakia has a positive balance of trade with the Czech lands in raw materials, chemicals, semifinished industrial products, and agricultural goods. The Czech lands have a positive balance in finished industrial and consumer goods, solid fuels, and electric energy. Economic recovery for the CSFR was widely forecast to begin in 1993. However, to the extent that the new republics are unable to use "domestic" and foreign sales to offset any decline in their two-way trade, the current recession will be more severe and last longer than predicted.

Analysts concur that the Czech lands are better equipped to shift from interrepublic trade to "domestic" and foreign trade. With their population of 10.4 million, the Czech lands form a larger "domestic" market than Slovakia's market of 5.3 million. The economic structure of the Czech lands is also better suited to prosper in world markets. About 80 percent of CSFR exports now come from the Czech lands and only 20 percent from Slovakia. Moreover, most of the CSFR tourist trade is in the Czech parts of the country. Slovakia's major export is arms, an industry whose shrinking global sales have made survival difficult even for developed country exporters. The Czech lands attract more foreign capital than Slovakia. About 80 percent of the estimated $1.2 billion foreign investment is in the Czech lands, and many analysts expect this ratio to increase as a result of separation. The Czechs have better infrastructure, and reportedly they have the most productive yet inexpensive labor force among the countries of Central and Eastern Europe (Bulgaria, Hungary, Poland, and Romania, in addition to the CSFR).

Various detailed assessments of the economic consequences of the split have emerged. According to the optimistic forecasts, which appear to be in the majority, the Czech economy will begin to recover in 1995, and the Slovak economy in 1996. However, several pessimistic predictions foresee further delays in the recovery of both economies, the accumulation of unmanageable amounts of domestic and foreign debt in Slovakia, and a trade war between the two nations. In support of the latter possibility, analysts cite the potentially explosive issue of interrepublic energy trade. The pipelines carrying Russian oil and gas to the Czech lands traverse the length of Slovakia. Should the Czechs decide to sell energy and fuel to the Slovaks at world market prices, some analysts point out, the Slovak Republic is likely to impose hard currency transit fees for the transport of oil and gas across its territory, thus provoking retaliation from the Czechs.

Since 1989, U.S. business with the CSFR has continued to grow, and U.S. firms doing or planning to do business with the Czechs and the Slovaks are apparently not discouraged by the new developments. U.S. trade with the CSFR increased from $133.4 million in 1989 to $265.6 million in 1991 and amounted to $226.4 million in the first 6 months of 1992. It is currently projected to reach half a billion dollars in the full year of 1992. (For details on U.S. trade with the CSFR, see USITC, *71st Quarterly Report, Trade Between the United States and the Former Soviet Union, Central and Eastern Europe, the Baltic Nations, and other Selected Countries During April-June 1992*, forthcoming later this month. Copies of the report can be obtained by calling 202-205-1809.) Although in mid-1992, actual U.S. direct investment in the CSFR amounted to only $60 to 80 million (5 to 7 percent of the estimated total direct investment of $1.2 billion), planned U.S. investment in the CSFR is reportedly in the range of $1.4 to 1.5 billion. U.S. direct investment is directly behind that of Germany, the largest provider of private capital throughout Central and Eastern Europe and the former Soviet Union.

U.S. businesses are already examining the opportunities that the decline of Czech and Slovak economic cooperation will create. As a result of the anticipated disruption in interrepublic commodity flows, U.S. importers may expect greater availability of semifinished goods (mostly metallurgical products) from Slovak suppliers and of finished products (textiles, shoes, and other manufactured goods) from Czech suppliers. From the point of view of U.S. exporters, opportunities could emerge for the sale of intermediate industrial goods, chemicals, and agricultural products to the Czech Republic. Opportunities to sell energy-generating equipment and machinery to produce finished industrial products could also emerge in the Slovak Republic.

The United States will consider the Czech and the Slovak republics bound by the bilateral treaties and agreements with the CSFR. Renegotiation of any treaty or agreement would be required only if a successor state indicated the need for it. An encouraging sign is that both republics gave assurances that they will honor the recently concluded U.S.-CSFR bilateral investment treaty (BIT). The BIT guarantees U.S. investors in both republics the opportunity to invest on terms no less favorable than those accorded to domestic or third country investors. It provides for the unconditional repatriation of capital, the protection of intellectual property rights, and access to international forums of arbitration.

In contrast to the anticipated future of U.S. relations with the Czech and Slovak republics, greater uncertainty surrounds the future of their relations with the European Community (EC) and with the other two Central European states of Hungary and Poland. The EC, which recently concluded an association agreement with the CSFR and opposed the split, might require the two successor states to renegotiate the accord as separate agreements. For the Czechs and the Slovaks, this requirement could delay their economic benefits derived from their integration into the Community. The anticipated split may also slow negotiations for the establishment of a free-trade area among the three Central European countries.

The Year in Trade

The deep divisions that have kept the GATT Uruguay Round of global trade talks from conclusion, the launching of the North American Free-Trade Agreement (NAFTA) negotiations, and the increasingly fractious relationship between trade and environmental issues are the special focus of the recently-released report by the ITC entitled *The Year in Trade: Operation of the Trade Agreements Program.* Covering calendar year 1991, *The Year in Trade* is one of the U.S. Government's most comprehensive annual guides to U.S. trade-related activities around the globe.

This year's report, the 43d in the series, also covers:

- other GATT activities, including actions of GATT dispute settlement panels on oilseeds, beer, and tuna;
- ongoing disagreements with major U.S. trading partners. Key issues are clearly explained, and 1991 developments chronicled. Featured are highly publicized disputes with the European Community over oilseeds, Airbus Industrie, meat, and corn gluten feed; with Canada over softwood lumber, pork, and beer; with Japan over semiconductors, automobiles, and major public works projects; and with Mexico over textile labelling rules.
- major developments in foreign policies that could potentially affect U.S. business. Among them are Canada's constitutional crisis, the EC's Maastricht treaty and 1992 integration program, Mexico's privatization efforts, and Korea's anti-import campaign.
- the operation of such programs as the President's Enterprise for the America's Initiative (EAI), the Caribbean Basin Economic Recovery Act (CBERA) and the U.S. Generalized System of Preferences (GSP), which provided duty-free entry for $13.4 billion in U.S. imports from more than 130 countries in 1991.

The Year in Trade also includes a wealth of statistical tables, as well as complete listings of antidumping, countervailing-duty, and other trade cases pursued by the U.S. Government in 1991. New in this year's report are the following:

- a concise overview of U.S. trade policy developments in the year and a handy, "Dates in Trade" chart;
- a redesigned, easy-to-read format; and
- an index geared to trade specialists that cross-references the report by country and commodity.

Copies of *The Year in Trade* may be obtained by calling (202) 205-1819, or from the Office of the Secretary, United States International Trade Commission, 500 E Street, SW, Washington, DC 20436. Requests to receive *The Year in Trade* on an annual basis should be made by calling (202) 205-3255 or by writing to the Office of Economics, Trade Reports Division, USITC, Washington, DC 20436. FAX requests may be made to (202) 205-2340.

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SPECIAL FOCUS
Economic Liberalization in South America: 1992 Update

Background

By 1991 most Latin American countries had turned away from decades of restrictive and protectionist economic policies and had initiated ambitious programs to liberalize their economies, as chronicled in a recent USITC report.[1] These reforms were lauded by President Bush in his announcement of the Enterprise for the Americas Initiative (EAI), a long-term U.S. program for economic cooperation and trade liberalization throughout the hemisphere.[2] Economic liberalization is necessary to make countries realistic candidates for the negotiation of free-trade agreements with the United States under the EAI, the Bush administration maintains.[3]

By yearend 1991, it was evident that economic reforms were being pursued faster and more successfully in some nations than in others. Countries such as Argentina, Bolivia, Chile, Colombia, Guatemala, Honduras, and Venezuela were making considerable headway in the drive to open their economies whereas others, such as Brazil, Costa Rica, Nicaragua, and Panama, were facing numerous obstacles to their reform efforts.

In recent months, some late bloomers like El Salvador and Ecuador have scored impressive gains in implementing economic reforms. In gereral terms, though, the pace of reforms in 1992 remains uneven despite the efforts to liberalize such policies on a regional basis and to establish regional free-trade areas through such associations as the Central American Common Market (CACM),[4] the Andean Group,[5] and the Southern Cone Common Market (MERCOSUR).[6] Moreover, while domestic economic and trade-related reforms already enacted generally remain in place, challenges to further reforms have emerged in a number of countries. In some countries, domestic economic reforms, such as the privatization of government-owned entities, are being met with political opposition and civil unrest. In others, the commitment to further trade and investment liberalization has been undercut by protracted economic instability or has been placed in doubt with the election of new political leaders.

This article identifies key economic developments and major policy changes in selected Central and South American countries so far during 1992.

Central American Countries

Costa Rica

Costa Rica was Central America's early leader in reducing trade barriers. A tariff regime introduced in 1986 reduced the average *ad valorem* tariff from 53 percent to 26 percent. A uniform 11 percent tariff was implemented (although numerous exceptions were allowed) following Costa Rica's November 1990 accession to the General Agreement on Tariffs and Trade (GATT). Slow progress in stabilizing the economy and reducing Costa Rica's reliance on tariffs and protectionist barriers brought further trade reforms to a virtual standstill during most of 1991, however. Other Central American countries, notably Guatemala and Honduras, rapidly eclipsed Costa Rica in the scope of their economic liberalization.

In late 1991, President Rafael Angel Calderón reinvigorated the trade liberalization process when he announced a plan to align Costa Rican tariffs with the common CACM tariff that is scheduled to become operative on January 1, 1993.[7] Accordingly, Costa

[1] USITC, *U.S. Market Access in Latin America: Recent Liberalization Measures and Remaining Barriers, With a Case Study on Chile*, USITC publication 2521, June 1992. This report is available by calling the Office of the Secretary on (202) 205-2000 (TDD terminal (202) 205-1809).

[2] "Remarks Announcing the Enterprise for the Americas Initiative," June 27, 1990, *Weekly Compilation of Presidential Documents*, vol. 26, No. 26, July 2, 1990, p. 1009.

[3] Julius L. Katz, Deputy U.S. Trade Representative, "Bush Administration Trade Policy," *Hemisphere*, Summer 1991, p. 12.

[4] CACM members are Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, and Panama.

[5] Andean Group members are Bolivia, Colombia, Ecuador, Peru, and Venezuela.

[6] MERCOSUR members are Argentina, Brazil, Paraguay, and Uruguay.

[7] The CACM common tariff will apply to products imported from outside Central America.

Rican tariffs were reduced for some 2,000 items not also produced in country in late February 1992, and for another 6,000 items in March. By the end of 1992, Costa Rica's tariffs will range from a minimum of 5 percent to a maximum of 20 percent.

For over one year, political rivalries in the Costa Rican legislative assembly have impeded the passage of a bill to permit the privatization of government-owned entities.[8] Until such legislation is passed, private investment remains strictly limited or banned in such key sectors as insurance, retail banking, hydrocarbons, utilities, ports, and most aspects of telecommunications.[9]

El Salvador

A late entry into the economic liberalization trend, El Salvador has made steady progress on a number of fronts. Since his June 1989 inauguration, President Alfredo Cristiani has introduced numerous domestic economic reforms and has liberalized the Salvadoran trade and investment regime.

The Cristiani administration unveiled a new tariff schedule following El Salvador's May 1991 accession to the GATT. With a few exceptions (notably luxury goods), tariffs range from a minimum of 5 percent to a maximum of 35 percent. The maximum tariff is scheduled to fall to 20 percent by the end of 1992 to conform with the CACM common tariff. To promote foreign investment, the government plans to create a one-stop-shop for foreign investors in 1993.

Improved domestic security conditions and an increase in economic activity since the signature of the January 1992 peace agreement have allowed the government to launch an ambitious privatization program. In July 1992 the Cristiani administration announced that it will sell the Hotel Presidente, one of the largest government-owned properties. The port authority and, pending legislative approval, the electric utility also will be offered for sale.[10]

Guatemala

President Jorge Serrano Elías has been the driving force for the liberalization of Guatemalan trade and investment policies since he assumed office in January 1991. Reforms have accelerated during 1992.

As part of Guatemala's October 1991 GATT accession, the Serrano administration agreed to eliminate nontariff barriers on over 100 products. Prior to that time, Guatemala already had reduced its tariffs on almost all manufactured goods to a range of 5 to 40 percent. Guatemala plans to lower its maximum tariff rate to a maximum of 20 percent by the end of 1992, in line with the CACM common tariff. The Serrano administration also plans to privatize a number of government-owned entities, beginning with the national telephone company and the government-owned railroad.[11]

Honduras

The rapid implementation of measures liberalizing the Honduran trade and investment regime has helped to make President Rafael Callejas a chief regional spokesperson of Central American economic integration efforts.

As a result of the economic reform program introduced by President Callejas in March 1990, the tariff structure was compressed from a range of 2 to 40 percent in 1990 to a range of 4 to 35 percent by January 1991. The maximum tariff was further reduced to 20 percent effective January 1, 1992, making Honduras the first country to implement the CACM common tariff.[12] The Honduran Government approved a new investment law in May 1992. Main features of the new law include transparent investment regulations, nondiscriminatory treatment for foreign investors, and a significantly reduced scope for discretionary government intervention.[13] In July, as a result of a successful exchange rate stabilization program, Honduras abandoned exchange controls that had been used to alleviate chronic foreign exchange shortages.[14]

Nicaragua

Key elements of President Violeta Chamorro's March 1991 economic stabilization program were the reduction of barriers to trade and investment and the privatization of government-owned entities. Although the Chamorro administration has enacted many economic reforms, inadequate protection for property owners continues to impede private investment in Nicaragua.

Since 1991, the Chamorro administration has liberalized the foreign investment regime to allow profit repatriation, implemented a streamlined tax system, and created new investment incentives, including the expansion of free trade zones. The tariff structure has been simplified and the maximum tariff reduced from 100 percent to 20 percent. The financial sector is being liberalized and the establishment of private banks authorized.[15]

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[8] Ronald Bailey, "Costa Rica Grapples With Privatization," *Times of the Americas*, Sept. 4, 1991, p. 10.

[9] USITC, *U.S. Market Access in Latin America*, p. 8-6 and EIU, *Nicaragua, Costa Rica, Panama: Country Report*, No. 3, 1992, p. 21.

[10] U.S. Department of State telegram, Aug. 25, 1992, San Salvador, message reference No. 08700.

[11] *Caribbean Update, Apr. 1991*, p. 11.

[12] Tom Welch, "Economic Policies Make Headway for U.S. Business in Honduras," *Business America*, Mar. 23, 1992, p. 11.

[13] "Honduras," *Caribbean Update*, August 1992, p. 12.

[14] "Export Market Controls Lifted," *Mexico and Central American Report*, July 16, 1992, p. 3.

Nicaragua's former Sandinista government expropriated private property throughout the country. The Chamorro administration has not yet implemented measures to protect property ownership and compensate for the Sandinista expropriations, reportedly making some private investors reluctant to increase their exposure in Nicaragua.[16] Notwithstanding strong opposition from organized labor, the Chamorro administration sold to private investors or closed 107 former government-owned entities in 1991 and plans to privatize at least that number in 1992. As part of the government's agreement with the unions, a 25 percent stake in each of the privatized companies will be reserved for workers.[17]

Panama

Liberalization of trade and investment regulations is a key element of President Guillermo Endara's economic reform program. Implementation is being slowed by civil unrest over social conditions and political infighting.

The December 1989 U.S. military action, which ended the Noriega regime and established a democratically elected government in Panama, gave President Endara the momentum to launch an ambitious economic reform program. To jump-start the Panamanian economy, President Endara has emphasized trade promotion and foreign investment incentives.

Panama is in the process of joining the GATT and already has begun to lower its tariffs. Panamanian tariffs remain among the highest in Central America, but are scheduled to fall to a maximum of 50 percent for agricultural products and 40 percent for industrial products by 1993. Even this reduction will leave Panamanian tariffs significantly above the 20 percent maximum tariff other CACM countries plan to implement effective January 1, 1993.

A long-awaited privatization law was signed, despite stiff political opposition, on July 14, 1992. The new bill requires that at least 45 percent of shares of government-owned firms must be sold on securities markets. The law excludes the telephone monopoly, the electricity utility, and the water company. This year alone, a cleaning and waste disposal company, a banana company, and an airline have been sold.

[16] U.S. Department of State telegram, Aug. 18, 1992, Managua, message reference No. 06834.

[17] EIU, *Nicaragua, Costa Rica, Panama: Country Report*, No. 2, 1992, p. 13.

South American Andean Countries

Bolivia

President Paz Zamora already has implemented among the most liberal trade and investment policies in Latin America despite the country's small size and few regionally competitive industries. The government launched new initiatives during 1992. Current reports indicate that the likely candidates for Bolivia's 1993 presidential election almost certainly would continue conservative and market-oriented economic policies.

Bolivia currently has the lowest and simplest tariff structure in the region, assessing ad valorem tariffs of 5 percent for capital goods and 10 percent for all other goods.[18] Bolivia will maintain this tariff structure for non-Andean products under the Andean Free-Trade Area (AFTA).[19] The current emphasis of the Paz Zamora administration is on expanding nontraditional exports and launching a privatization program. The Bolivian Government hopes that export incentives will contribute to increased production of nontraditional agricultural exports and stem the production of coca leaves, the raw material for cocaine. In April 1992, the Bolivian Government opened its first "single exporters' window" in the capital city, La Paz. Other such one-stop-shop facilities for exporters will be established throughout the country.

In April 1992, Bolivia enacted a privatization law that allows the government to sell off its nonstrategic monopolies. Natural resource entities, such as the government-owned mining and petroleum companies, will not be eligible, whereas the telecommunications and railway companies will be privatized only if the new owners promise to break up the monopolies in these sectors.[20] The first highly visible privatization was scheduled to be the sale of the national airline Lloyd Aéro Boliviano (LAB), but an August 1992 call for bids netted only one potential investor, Spain's Iberia Airlines. Iberia offered far below what the Bolivian Government had expected, and the sale was subsequently postponed. On August 19, 1992 the Paz Zamora administration signed an agreement with the Bolivian Armed Forces that eventually will lead to the privatization of military assets. The Bolivian Armed Forces currently operate a number of civilian production facilities and services.[21]

[18] USITC, *U.S. Market Access in Latin America*, p. 6-6.

[19] The AFTA became operative for Bolivia, Colombia, and Venezuela on Jan. 1, 1992.

[20] "Bolivia Approves Privatization Law," *Latin America/Caribbean Business Bulletin*, July 1992, p. 4.

[21] "Bolivia: Privatizations," *Latin American Weekly Report*, Sept. 3, 1992, pp. 4-5.

Colombia

Trade and investment barriers have been reduced under the economic liberalization plan known as *apertura* implemented by President César Gavira after he took office in August 1990. Colombia's efficient, trade-based economy and track-record of political stability—despite the disruptions caused by drug traffickers and terrorist attacks—make it unlikely that President Gavira's reforms will be adversely affected by economic setbacks. However, the Gavira administration's privatization program has lost momentum in recent months.

Under the Gavira administration, Colombia has reformed its trade, investment, and foreign exchange regimes. New laws eliminate almost all prior import license requirements, simplify import and export procedures, establish a free market exchange regime, and create transparent and more liberal foreign investment rules.[22] Colombia has reduced its tariffs and implemented the simplified four-tier tariff structure that all Andean countries (except Bolivia) are to apply to non-Andean products under the AFTA. These tariff levels are 0 percent for primary goods, inputs, and capital goods not produced in country; 5 to 10 percent for primary goods and capital goods produced in country; and 15 percent for final consumer goods

Colombia's economy received a severe shock during 1992. A drought, caused by shifts in the El Niño Pacific Ocean current, drained the water level in the reservoirs that provide hydroelectric power for much of the country. This forced the government to impose mandatory electricity blackouts lasting up to ten hours a day. Although the blackouts were partly suspended in August 1992, daily nationwide power cuts remain in place as of this writing and may continue into 1993. The electricity crisis is causing financial hardship for many Colombian businesses.

Colombia's privatization program has lost momentum. Financial hardship caused by the electricity crisis has made many once profitable entities less attractive candidates for investors. In April 1992, violent labor strikes protesting the government's plan to privatize the telecommunications monopoly (one of the government's remaining profit-making assets) forced President Gavira to declare a 3-day state of emergency and to suspend the sale. A more significant setback occurred in August, when it was reported that the implementing legislation for the Gavira administration's privatization program was found to be unconstitutional.[23]

Ecuador

After lagging behind other Andean countries in implementing economic reforms, Ecuador finally lowered tariffs and simplified its tariff structure in May 1992. More far-reaching structural reforms may take longer since President Sixto Durán Ballén, who was inaugurated in August, concentrates on stabilizing Ecuador's economy.

The new tariff structure announced on May 28, 1992, completed the Rodrigo Borja administration's tariff reduction program. The structure is in line with the AFTA common tariff, ranging from a minimum of 5 percent to a maximum of 20 percent. Automobiles will continue to face a 40 percent tariff.[24] Ecuador will formally join the AFTA in October 1992. In doing so, Ecuador will eliminate tariffs on 75 percent of its trade with Bolivia and Colombia and on 50 percent of its trade with Venezuela.[25]

President Durán announced an economic adjustment plan on September 4, 1992. The plan focuses on combatting inflation, reducing the fiscal deficit, and raising extra revenues for public works. The Durán administration also stated that it will submit draft legislation to the congress to allow the privatization of some government-owned entities.[26]

Peru

A domestic political crisis, prompted when President Alberto Fujimori suspended constitutional rule, has derailed Peru's short-lived economic reform program. Peru's economy has been weakened by years of policy mismanagement and held hostage by drug traffickers and the Sendero Luminoso (Shining Path) insurgents. The September 1992 capture of the insurgent leader could signal a sea change for Peru's economic future.

On April 5, 1992, President Fujimori suspended the constitution, dissolved the congress, and announced the installation of a government of national emergency. President Fujimori stated that this so-called *autogolpe* ("self-coup") was necessary to combat rampant insurgent activity and to restore economic growth. Plans to return to democratic rule, including a national referendum to elect a constituent assembly, already have been postponed twice and are now scheduled for November 1992.

The *autogolpe* derailed the Fujimori administration's far-reaching economic reform program. Under the program, Peru implemented a three-tier tariff structure with rates of 50 percent, 25 percent, and 15 percent and planned for further tariff reductions.[27] Peru also eliminated import permits and foreign exchange controls and launched an ambitious

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22 U.S. Department of State telegram, Sept. 30, 1991, Bogota, message reference No. 15167.

23 "Crisis Worsens at Gavira's Mid-Term," *Latin American Weekly Report*, Aug. 27, 1992, p. 4.

24 U.S. Department of State telegram, June 1, 1992, Quito, message reference No. 05368.

25 U.S. Department of State telegram, Aug. 27, 1992, Quito, message reference No. 08149.

26 "Sixto Durán Unveils Adjustment Plan," *Latin American Weekly Report*, Sept. 17, 1992, p. 4.

27 Inter-American Development Bank, *Economic and Social Progress in Latin America: 1991 Report* (Washington, DC: The Johns Hopkins University Press, 1991), p. 148.

privatization program to sell off up to 200 government-owned entities.[28]

Since the suspension of constitutional rule, both tariff reform and the gradual alignment of Peru's tariff structure with the AFTA common tariff have ceased. Colombia broke economic relations, and Venezuela severed diplomatic ties with Peru following *autogolpe*. In August 1992, Peru announced its temporarily withdrawal from Andean Group trade arrangements until December 31, 1993, when it is scheduled to resume as a full member of the AFTA.[29]

The *autogolpe* also complicated Peru's privatization program. President Fujimori had hoped to launch this program with sales of the government-owned airline, a mining company, and a chemical company. However, potential investors reportedly are now reluctant to acquire Peruvian assets. The concern is that a subsequent constitutionally elected administration might overrule actions undertaken by the extra-constitutional Fujimori regime or fail to recognize transactions executed during this period. The Peruvian administration nevertheless remains confident that the privatization program will advance.[30]

Venezuela

Under President Carlos Andrés Pérez, Venezuela has significantly opened its trade and investment regimes. President Pérez remains committed to seeing Venezuela through another year of economic austerity measures and a cost-cutting privatization program despite the backlash evidenced in antigovernment protests.

As part of its September 1990 accession to the GATT, Venezuela bound its tariffs to a maximum of 50 percent—although lower rates of 15 to 35 percent were applied for several hundred tariff lines—and agreed to reduce its tariffs to a maximum of 20 percent by 1993. The maximum tariff rate was lowered to 20 percent effective March 16, 1992, allowing Venezuela to implement the AFTA common tariff one year ahead of schedule. This marked the completion of the tariff reform program the Pérez administration had set out to accomplish. The administration has stated that it will leave further changes to the tariff schedule until after a new president is elected in December 1993.[31]

The Pérez administration's austerity program is the source of much public discontent. An unsuccessful February 1992 military coup attempt was inspired in part by discontent over the sharp decline in the military budget. The privatization program is generating equally violent reactions from civilian workers. Labor unrest has prompted the government to dispatch militia to several cities this year to restore order. Despite the domestic social unrest, President Pérez is pressing ahead with privatization. So far in 1992, Venezuela has privatized two sugar mills and has plans to sell two electricity generating companies and the airline Aeropostal. Moreover, on August 23, 1992, President Pérez announced a new austerity program which further slashes government expenses through draconian cuts in the budget of the government-owned oil company. He also confirmed plans to privatize the aluminum firm as well as other government-owned companies in agriculture, tourism, transport, power generation, mining, steel, and finance during 1992 and 1993.[32]

Other South American Countries

Argentina

Argentina continues to benefit from the economic reforms being implemented by President Carlos Menem and his finance minister, Domingo Cavallo. These reforms have increased economic stability, opened the Argentine economy to foreign trade and investment, and renewed public and international confidence in Argentina's prospects. The Argentine Government's forced repurchase of shares of the country's international airline in July 1992 marked the first setback for an ambitious privatization program.

By making the Argentine currency fully convertible into U.S. dollars and backing the currency by gold and foreign-currency reserves, the Menem administration has effectively eliminated Argentina's once-crippling budget deficit. Tariffs have been significantly reduced. Current tariff rates are 5 percent for goods also produced in country, 13 percent for raw materials and intermediate products, 22 percent for finished products, and 35 percent for special products such as electronics.[33] Argentina thus already meets the MERCOSUR common tariff guidelines, which call for members to implement an average tariff level of 14.2 percent and a maximum rate of 35 percent by March 1993.[34]

A review of Argentine trade policies completed by the GATT Council in March 1992 commended the transformation of Argentina "from a highly protected and regulated economy into one of the most open in

[28] Pacific Basin Economic Council, "Privatization Opportunities in Peru," *International Bulletin*, July 15, 1992.

[29] "Slower Pace for Subregional Groups," *Latin American Weekly Report*, Sept. 10, 1992, p. 6 and U.S. Department of State telegram, Sept. 16, 1992, Lima, message reference No. 12349.

[30] U.S. Department of State telegram, Sept. 11, 1992, Lima, message reference No. 12144.

[31] U.S. Department of State, April 7, 1992, Caracas, message reference No. 03879.

[32] "Three Years On, Carlos Andrés Pérez Launches a New Belt-Tightening Package," *Latin American Weekly Report*, Sept. 3, 1992, p. 1.

[33] GATT Secretariat, *Trade Policy Review Mechanism: Argentina*, C/RM/S/18A, Nov. 8, 1991, p. 68.

[34] "Presidents Set Timetable for MERCOSUR," *Southern Cone Report*, Aug. 6, 1992, p. 1.

the world."[35] The GATT Council noted that most of the tariff and nontariff barriers that had been used extensively to support Argentina's manufacturing sector had been eliminated or suspended pending ongoing review by the Menem administration. The GATT review specifically praised Argentina's tariff reductions, the virtual elimination of quantitative restrictions, deregulation of the internal market and the extensive privatization program.

A setback for Argentina's privatization program occurred when the government was forced to repurchase shares of the airline Aerolíneas Argentinas. Argentine and foreign private investors originally purchased 85 percent of the airline when it was sold barely one year ago. In July 1992, the Argentine Government bought back 28 percent of the company from financially pressed Argentine minority shareholders.[36] This setback may cause Argentina to scrutinize its privatization program and potential investors.

Brazil

The Brazilian Government has significantly liberalized its trade and investment policies. However, the administration's failure to stabilize the economy and the ongoing impeachment trial of President Fernando Collor de Mello could seriously jeopardize Brazil's ability to advance reforms. The setbacks put into question MERCOSUR's ability to meet its timetable for regional trade liberalization and closer economic cooperation among members over the next few years.

In January 1992, the Brazilian Government implemented the second phase of a 4-year tariff reduction plan begun 1 year earlier. This second round of tariff reductions affected over 12,000 items and reduced the weighted average ad valorem tariff from 25.3 percent to 21.2 percent. The average tariff level is scheduled to fall to 17.1 percent on October 1, 1992, and to 14.2 percent on July 1, 1993, when a maximum tariff of 35 percent also is to be implemented to align the Brazilian tariff structure with the MERCOSUR common tariff.[37]

The Collor administration also has lifted many nontariff barriers and made the approval of import licenses virtually automatic. Effective October 1992, restrictions on imports of computer products are scheduled to be lifted. A privatization program continues on track, although there have been several delays. Ten firms have been privatized since the program got under way in October 1991, moving some 25,000 jobs into the private sector and generating some $2.8 billion in earnings for the Brazilian Government.

Presidential impeachment proceedings against Fernando Collor on corruption charges have not yet had an adverse impact on Brazil's economy. (On September 29, 1992 the Brazilian Congress voted to initiate an impeachment trial. The vote required Fernando Collor to relinquish his position for 6 months—Vice President Itamar Franco will assume the presidency—pending the outcome of the impeachment trial.) The acting government's lack of a clear mandate, however, could bring policymaking in Brazil to a standstill. Meanwhile, Brazil's MERCOSUR partners are increasingly concerned that a failure to stabilize the Brazilian economy will impede regional economic integration plans (all members have pledged to implement a common tariff structure by March 1993 and to begin coordinating macroeconomic policies by January 1995) and derail all hopes for ultimately securing a free-trade agreement with the United States.[38]

Chile

President Patricio Aylwin continues to reinforce Chile's long-standing commitment to low tariffs and few restrictions on foreign investment. Chile also is pursuing bilateral free-trade agreements with other reform-oriented countries. Pragmatic market-oriented economic policies are not likely to change between now and the December 1993 presidential election.

Chile applies a uniform tariff to most imports. The tariff was reduced from 15 percent to 11 percent in May 1991. Chile permits foreign ownership in almost all sectors of its economy and, for years, has had one of the most transparent and nondiscriminatory trade and investment regimes in Latin America. On April 29, 1992, the Chilean congress approved a new law which allows the national copper company to engage in joint ventures with local or foreign private investors.

Chile continues to eschew participation in regional trade arrangements despite invitations to apply for membership from both the Andean Group and the MERCOSUR countries. Chile is negotiating bilaterally with countries that are pursuing economic reforms and liberalization. A free-trade agreement (FTA) with Mexico became operative in October 1991, covering 94 percent of their bilateral trade. During negotiations with Venezuela in late 1991 for a bilateral FTA, the two nations agreed in principle to gradual tariff reduction after 1994 but were at an impasse over the list of products to be excluded from tariff reductions. Chile signed an economic framework agreement with Colombia in 1992, but no further negotiations have occurred.[39] The Chilean Government has actively sought for nearly 1 year to commence negotiations for an FTA with the United States. The Bush administration has stated that negotiations for United States-Chile FTA will be the next item on the U.S. hemispheric trade agenda after the conclusion of negotiations for the NAFTA.

[35] U.S. Department of State telegram, Mar. 10, 1992, Geneva, message reference No. 02052.

[36] "Major Setback with Aerolíneas Sell-Off," *Southern Cone Report*, Sept. 10, 1992, p. 1.

[37] U.S. Department of State telegram, Mar. 28, 1992, Washington, D.C., message reference No. 097384.

[38] Stephen Fidler, "Brazilian Economy Paces MERCOSUR's Tariffs Timetable," *Financial Times*, June 23, 1992, p. 3.

[39] U.S. Department of State telegram, June 23, 1992, Santiago, message reference No. 04860.

STATISTICAL TABLES

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Industrial production, by selected countries and by specified periods, January 1989-May 1992

(Percentage change from previous period, seasonally adjusted at annual rate)

				1991					1992					
Country	*1989*	*1990*	*1991*	*III*	*IV*	*Oct.*	*Nov.*	*Dec.*	*I*	*Jan.*	*Feb.*	*Mar.*	*Apr.*	*May*
United States	2.6	1.0	-1.9	6.8	-0.7	0	-3.3	-7.5	-3.1	-8.6	7.0	5.7	4.5	8.1
Japan	6.2	4.5	2.1	1.3	-5.1	-0.9	0	-14.9	-11.7	-13.4	-5.6	-27.0	8.3	-25.2
Canada	2.0	0.3	-1.1	-3.3	-2.1	0	-1.1	-1.1	2.3	1.1	-9.3	2.2	-2.2	5.7
Germany	5.3	5.9	3.2	-4.7	-2.9	-5.7	-1.0	-13.8	4.6	11.5	22.8	-11.9	(1)	(1)
United Kingdom	0.3	-0.6	-3.0	4.2	-0.5	8.2	-5.5	-4.4	-3.7	-10.8	-14.6	-9.7	8.3	(1)
France	3.7	1.3	0.6	2.0	-1.4	14.7	-8.1	-13.8	0.6	22.2	-9.1	-2.1	19.6	(1)
Italy	3.9	-0.6	-1.8	-9.1	-2.0	-3.1	25.6	-31.3	3.1	24.7	9.8	-2.0	-10.8	(1)

[1] Not available.

Note.—Data presented for Germany includes information only for what was once West Germany. When data for the combined Germanies are available they will be used.

Source: *Economic and Energy Indicators*, U.S. Central Intelligence Agency, July 17, 1992.

Consumer prices, by selected countries and by specified periods, January 1989-June 92

(Percentage change from previous period, seasonally adjusted at annual rate)

				1991				1992							
Country	*1989*	*1990*	*1991*	*IV*	*Oct.*	*Nov.*	*Dec.*	*I*	*II*	*Jan.*	*Feb.*	*Mar.*	*Apr.*	*May*	*Jun.*
United States	4.8	5.4	4.2	3.6	0.9	4.5	2.6	2.8	(1)	0.9	3.5	6.2	2.6	1.7	(1)
Japan	2.3	3.1	3.3	3.8	7.7	9.0	-0.9	1.5	2.6	-1.5	1.0	2.6	4.9	-1.0	4.9
Canada	5.0	4.8	5.6	0.2	-2.8	2.9	0	1.6	(1)	1.0	1.9	4.8	1.9	-0.9	(1)
Germany	2.8	2.7	3.5	3.4	3.3	5.5	1.1	3.0	(1)	0	6.6	6.5	1.1	5.4	(1)
United Kingdom	7.8	9.5	5.9	4.0	3.7	5.3	5.9	4.3	4.0	3.3	4.0	4.0	5.0	4.1	0.7
France	3.5	3.4	3.1	3.5	3.7	4.2	3.7	3.2	(1)	2.4	3.5	3.3	1.7	3.2	(1)
Italy	6.6	6.1	6.5	5.7	5.7	7.2	4.5	5.0	5.6	7.7	-0.5	6.6	5.6	8.6	4.6

[1] Not available.

Note.—Data presented for Germany includes information only for what was once West Germany. When data for the combined Germanies are available they will be used.

Source: *Economic and Energy Indicators*, U.S. Central Intelligence Agency, July 17, 1992.

Unemployment rates, (civilian labor force basis)[1] by selected countries and by specified periods, January 1989-July 1992

				1991	1992								
Country	*1989*	*1990*	*1991*	*IV*	*I*	*II*	*Jan.*	*Feb.*	*Mar.*	*Apr.*	*May*	*Jun.*	*Jul.*
United States	5.3	5.5	6.7	6.9	7.2	7.5	7.1	7.3	7.3	7.2	7.5	7.8	7.7
Japan	2.3	2.1	2.1	2.2	2.1	(5)	2.1	2.0	2.1	2.0	2.1	(5)	(5)
Canada	7.5	8.1	10.3	10.3	10.7	11.3	10.4	10.6	11.1	11.0	11.2	11.6	11.6
Germany[2]	5.7	5.2	4.4	4.4	4.4	4.6	4.4	4.4	4.4	4.6	4.6	4.7	4.7
United Kingdom	7.1	6.9	8.9	9.8	10.2	10.5	10.1	10.3	10.3	10.4	10.5	10.6	10.7
France	9.6	9.2	9.8	10.3	10.0	10.2	10.1	10.1	10.1	10.2	10.2	10.3	(5)
Italy[3]	7.8	7.0	6.9	6.9	7.0	(4)	7.0	(4)	(4)	(4)	(4)	(4)	(4)

[1] Seasonally adjusted; rates of foreign countries adjusted to be comparable with the U.S. rate.

[2] Formerly West Germany.

[3] Many Italians reported as unemployed did not actively seek work in the past 30 days, and they have been excluded for comparability with U.S. concepts. Inclusion of such persons would increase the unemployment rate to 11-12 percent in 1989-1990.

[4] Italian unemployment surveys are conducted only once a quarter, in the first month of the quarter.

[5] Not available.

Source: *Unemployment Rates in Nine Countries*, U.S. Department of Labor, September 1992.

Money-market interest rates,[1] by selected countries and by specified periods, January 1989-August 1992

(Percentage, annual rates)

Country	1989	1990	1991	1991 IV	1991 Dec.	1992 I	1992 II	1992 Jan.	1992 Feb.	1992 Mar.	1992 Apr.	1992 May	1992 Jun.	1992 Jul.	1992 Aug.
United States	9.3	8.3	5.9	5.0	4.4	4.2	3.9	4.5	4.1	4.4	4.0	3.8	3.9	3.4	3.3
Japan	5.3	6.9	7.5	7.2	7.0	6.6	6.4	6.8	6.6	6.5	6.3	6.3	6.3	(2)	(2)
Canada	12.2	13.0	9.0	7.8	7.5	7.3	6.5	7.3	7.3	7.5	6.9	6.5	5.9	(2)	(2)
Germany	7.1	8.5	9.2	9.5	9.6	9.6	9.8	9.5	9.6	9.6	9.9	9.7	9.6	(2)	(2)
United Kingdom	13.9	14.8	11.5	10.6	10.8	10.5	10.2	10.6	10.4	10.7	10.4	10.0	10.0	(2)	(2)
France	9.4	10.3	9.6	9.6	10.1	9.9	9.9	9.9	9.9	10.0	9.9	9.9	10.0	(2)	(2)
Italy	12.8	12.7	12.1	12.0	12.6	12.2	12.9	12.1	12.2	12.3	12.4	12.4	13.7	(2)	(2)

1 90-day certificate of deposit.

2 Not available.

Note.—Data presented for Germany includes information only for what was once West Germany. When data for the combined Germanies are available they will be used.

Source: *Federal Reserve Statistical Release*, September 8, 1992, and *Economic and Energy Indicators*, Central Intelligence Agency, July 17, 1992.

Effective exchange rates of the U.S. dollar, by specified periods, January 1989-August 1992

(Percentage change from previous period)

Item	1989	1990	1991	1991 IV	1992 I	1992 II	1992 Jan.	1992 Feb.	1992 Mar.	1992 Apr.	1992 May	1992 Jun.	1992 Jul.	1992 Aug.
Unadjusted:														
Index[1]	91.3	86.5	85.5	84.0	84.8	85.2	83.0	84.8	86.8	86.4	85.5	83.7	81.7	80.9
Percentage change	6.4	-5.3	-1.2	-4.1	.8	.4	.2	2.1	2.3	-.4	-1.0	-2.1	-2.4	-.9
Adjusted: Index[1]	91.8	88.1	87.0	85.6	86.7	86.9	84.6	86.4	88.6	88.2	87.3	85.4	83.3	82.7
Percentage change	6.8	-4.0	-1.2	-3.2	1.3	.2	.2	3.1	2.5	-.4	-1.0	-2.2	-2.4	-.7

1 1980-82 average=100.

Note.—The foreign-currency value of the U.S. dollar is a trade-weighted average in terms of the currencies of 15 other major nations. The inflation-adjusted measure shows the change in the dollar's value after adjusting for the inflation rates in the United States and in other nations; thus, a decline in this measure suggests an increase in U.S. price competitiveness.

Source: Morgan Guaranty Trust Co.of New York, September 1992.

Trade balances, by selected countries and by specified periods, January 1989-July 1992

(In billions of U.S. dollars, f.o.b. basis, at an annual rate)

				1991	1992						
Country	*1989*	*1990*	*1991*	*IV*	*I*	*II*	*Mar.*	*Apr.*	*May*	*Jun.*	*Jul.*
United States[1]	-109.1	-101.7	-66.2	-66.8	-59.6	-83.2	-67.0	-84.7	-85.6	-80.7	-93.9
Japan	77.6	63.7	103.1	119.6	130.4	([3])	128.4	111.6	142.8	([3])	([3])
Canada	6.0	9.4	6.4	3.2	7.2	([3])	7.2	7.2	([3])	([3])	([3])
Germany[2]	71.9	65.6	13.5	29.2	([3])	([3])	([3])	([3])	([3])	([3])	([3])
United Kingdom	-40.4	-33.3	-17.9	-18.0	-21.6	([3])	-18.0	-28.8	-18.0	([3])	([3])
France	-7.0	-9.2	-5.4	1.2	3.6	([3])	2.4	16.8	9.6	([3])	([3])
Italy	-12.9	-10.0	-12.8	-10.8	-10.0	([3])	-4.8	-15.6	-15.6	([3])	([3])

[1] Figures are adjusted to reflect change in U.S. Department of Commerce reporting of imports at customs value, seasonally adjusted, rather than c.i.f.value.

[2] Imports, c.i.f value, adjusted.

[3] Not available.

Note.—Data presented for Germany includes information only for what was once West Germany. When data for the combined Germanies are available they will be used.

Source: *Economic and Energy Indicators*, U.S. Central Intelligence Agency, July 17, 1992 and *Advance Report on U.S. Merchandise Trade*, U.S. Department of Commerce, September 17, 1992.

U.S. trade balance,[1] by major commodity categories,and by specified periods, January 1989-July 1992

(In billions of dollars)

				1991	1992						
Country	*1989*	*1990*	*1991*	*IV*	*I*	*II*	*Mar.*	*Apr.*	*May*	*Jun.*	*Jul.*
Commodity categories:											
Agriculture	17.9	16.3	16.2	5.4	5.1	3.7	1.6	1.5	1.1	1.1	1.3
Petroleum and selected product—(unadjusted)	-44.7	-54.6	-42.3	10.0	-8.1	-10.8	-2.9	-3.3	-3.5	-4.0	-4.2
Manufactured goods	-103.2	-90.1	-67.2	-21.5	-14.5	-16.9	-4.9	-5.8	-5.3	-5.7	-9.7
Selected countries:											
Western Europe	-1.3	4.0	16.1	3.3	6.6	1.4	2.3	.6	.9	-.1	-1.1
Canada[2]	-9.6	-7.7	-6.0	-2.1	-1.4	-1.8	-.5	-.6	-.8	-.4	-.4
Japan	-49.0	-41.0	-43.4	-12.4	-10.8	-11.1	-4.0	-4.2	-3.5	-3.4	-3.9
OPEC (unadjusted)	-17.3	-24.3	-13.8	-2.5	-1.5	-2.2	-.4	-.3	-.8	-1.1	-1.5
Unit value of U.S.imports of petroleum and selected products (unadjusted)	$16.80	$19.75	$17.49	$17.52	$14.57	$16.82	$14.46	$15.49	$16.72	$18.25	$18.18

[1] Exports, f.a.s. value, unadjusted. Imports, customs value, unadjusted.

[2] Beginning with 1989, figures include previously undocumented exports to Canada.

Source: Advance Report on U.S. Merchandise Trade, U.S. Department of Commerce, September 17, 1992.

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